Supreme Court, U. S.
FILED
DEC 19 1979
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-962

TENNESSEE GAS PIPELINE COMPANY,
a Division of Tenneco Inc.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Tennessee Gas Pipeline Company, a Division of Tenneco Inc. (Tennessee), hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered in the above-captioned case on June 20, 1979.

OPINIONS BELOW

The opinion of the Court of Appeals (Appendix A, *infra*) has not yet been officially reported. Opinion Nos. 769 (Appendix B, *infra*) and 769-A (Appendix

C, *infra*), of the Federal Power Commission (Commission)[1] are not yet reported.

JURISDICTION

The judgment of the Court of Appeals was entered on June 20, 1979, and orders denying timely petitions for rehearing and suggestions for rehearing *en banc* were issued on October 31, 1979 (Appendix D, *infra*). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. § 717r(b).

QUESTION PRESENTED

Whether, in determining the jurisdictional rates to be charged by natural gas pipeline companies under the Natural Gas Act, the Commission may, by retroactively imposing a timing limitation between the date of the pipelines' advance payments and related producer expenditures under advance payments contracts entered into pursuant to the Commission's Order No. 465, exclude such advance payments from the pipelines' rate base and thereby deny them recovery of the substantial capital carrying costs associated with these advances.

REGULATION INVOLVED

The Commission's Order No. 465, 48 FPC 1550 (1972), is set out in Appendix E, *infra*.

[1] The Federal Power Commission was superseded as of October, 1977 by the Federal Energy Regulatory Commission with most of its functions including those here involved transferred to the new Commission. See Department of Energy Reorganization Act of 1977, 42 U.S.C. §§ 7107, 7172(a)(1)(B), (C).

STATEMENT OF THE CASE

Tennessee is a natural gas pipeline company subject to the Commission's regulation under the Natural Gas Act.[2] By its rate Opinion Nos. 769 and 769-A, the Commission reduced Tennessee's rates by excluding from Tennessee's rate base more than $100,000,000 of advance payments made by Tennesseee to producers pursuant to agreements entered into under the Commission's advance payments program to obtain commitments for gas supply for the purpose of alleviating the gas supply shortages on its system. All of the advance payments in question were made under agreements between Tennessee and the producers during 1973 when the Commission's Order No. 465 governed the advance payments program. These agreements required that the advance payments be made on a front-end, or lump sum basis, which was typical of virtually all of the advance payment agreements between pipelines and producers as of that time.[3] As recognized by the court below, almost 99 percent of the total of $5.5 billion committed by interstate pipelines under the advance payments program was of the front-end type involved in this case.

While neither Order No. 465, nor any of the prior advance payment orders, prohibited front-end type

[2] Tennessee's gas pipeline system extends from gas supply sources in Texas, Louisiana and the offshore area of the Gulf of Mexico northeastward through sixteen states terminating in New England. It delivers over one-trillion cubic feet of gas annually to its customers. For more than a decade, Tennessee has been unable annually to contract for new gas reserves in sufficient quantities to offset its annual sales.

[3] Front-end or lump sum advances are those made to the producer at or about the time the advance payment agreement is entered into.

advances, the Commission held for the first time in the rate orders here under review that front-end advance payments were "presumptively extravagant" and excluded from Tennessee's rate base those advance payments which had not been expended by the producer within 30 days after the close of the rate case test period. Upon review, the court below held that it was not impermissable retroactive rule-making for the Commission to read into Order No. 465 a timing requirement between the date of the advance and the date of the producer expenditure, but that the 30-day rule was improper and unsupported. The court, therefore remanded the case for a determination of a proper timing requirement.

Two days after the opinion of the court below, the Court of Appeals for the Fifth Circuit in *United Gas Pipeline Company* v. *F.E.R.C.*, 597 F.2d 581 (1979), *reversed* a Commission rate order which had excluded from United's rate base front-end type advance payments virtually identical to Tennessee's and made by United to producers under agreements also governed by Order No. 465. The Fifth Circuit held that "[t]he law will not tolerate this sort of after-the-fact, in fact retroactive, imposition of standards" (597 F.2d at 586).

A. Background

Order No. 465 is the fourth in a series of five orders issued as part of an advance payments program undertaken by the Commission and directed toward alleviation of the natural gas shortage.[4] The program, which

[4] Order No. 410, 44 FPC 1142 (1970); Order No. 410-A, 45 FPC 135 (1971); Order No. 441, 46 FPC 1178 (1971); Order No. 465, 48 FPC 1550 (1972); Order No. 499, 50 FPC 2111 (1973).

was initiated by the Commission with the issuance of Order No. 410 in October, 1970, was designed to provide an incentive to natural gas pipelines to advance capital to producers for use in exploration, lease acquisition, development or production of natural gas in exchange for a commitment of the discovered and developed gas reserves to the pipeline making the advances. In order to compensate the pipelines for their carrying costs in making these advance payments, the Commission from the outset recognized the need to permit the pipelines to include such advance payments in their rate base upon which they would receive the fair rate of return equal to the pipelines' weighted average cost of capital (44 FPC at 1144).[5]

From the outset, the Commission required that copies of all advance payment agreements be filed by pipelines with the Commission so that it could monitor the program. While the program was in effect,[6] the Commission periodically reviewed and evaluated the program, in order to determine whether and to what extent it should be continued and/or modified. In connection with such review, the Commission prescribed that each of the several advance payments orders apply to advance payment agreements made during a specific period and, as the program progressed, the Commission

[5] The program was conditionally approved by the Court of Appeals for the District of Columbia Circuit in *Public Service Commission for the State of New York* v. *F.P.C.*, 467 F.2d 361 (1972), as a "justifiable experiment in the continuing search for solutions to our nation's critical shortage of natural gas" (467 F.2d at 371).

[6] The Commission prospectively terminated the program as of December 31, 1975. Order on Remand From Court Opinion Terminating Investigation and Terminating Advance Payment Program With Conditions, 54 FPC 3046 (1975).

prescribed modifications which were in all instances to be applied *prospectively* only to new agreements governed by each new order.

Order No. 465 here involved applied to advance payment agreements entered into during the calendar year 1973. As recognized by the court below (App. A, p. 19a),[7] there is no question that the advance payments here involved complied with the express conditions of that Order.

When Tennessee entered into its Order No. 465 advance payment agreements, it had no reason to believe that Order No. 465 imposed any timing requirement between the date of the advance payment and the date of the producer expenditure so as to preclude front-end advances. As stated above, neither Order No. 465 nor any of the prior advance payment orders contained any such requirement or prohibition, although timing requirements were expressly contained as to other matters.[8] The Commission was fully aware that, from the inception of the program in 1970, the vast bulk of the advance payment agreements being entered into called for front-end advances since all of these agreements were required to be filed with the Commission for its review. In fact, the Public Service Commission of New York specifically advised the Commission, in its comments to the Commission with regard to the then-proposed Order No. 465, of the magnitude of the advances being made by pipelines, indicating that they were being made "*at once,*" and it urged the Commission to established guidelines which would tie

[7] "App." refers to the appendices to this petition which are printed in a separate volume.

[8] For example, Order No. 441 required repayment of the advance payments by the producers to begin within five years of inclusion of the advance payment in rate base (46 FPC at 1180).

the advances included in rate base to "specific drilling cost expenditures" (JA 262-264, 268).[9] The Commission not only declined to adopt New York's request in Order No. 465, but rejected New York's renewal of that request on rehearing (48 FPC at 1550; Order of Clarification and Denial of Rehearing or Modification, 49 FPC 517 (1973)).

It was not until Order No. 499 was issued on December 29, 1973, after all the advance payment agreements in question were executed, that the Commission, for the very first time, established any rule concerning the temporal relationship between the advance payment and the producer expenditures. The Commission specifically provided in Order No. 499 that its requirements would apply prospectively only (50 FPC at 2116).

Prior to Order No. 499, there was no suggestion of an advance-expenditure timing requirement in any of the decisions issued by the Commission or its Administrative Law Judges. See *e.g., Columbia Gas transmission Company,* Opinion No. 722, 53 FPC 708 (1975); *Transcontinental Gas Pipe Line Corp.,* 47 FPC 293 (1972) (*Transco*); *Transcontinental Gas Pipe Line Corp.,* Order Approving Amendment to Agreement as to Rates, Docket No. RP71-31, pp. 2-3 (July 30, 1971).[10] In *Transco,* the Commission ap-

[9] "JA" references are to the Joint Appendix below containing the stipulated portions of the record before the Commission deemed to be relevant to the issues.

[10] There also are a number of unreported Commission orders sanctioning without discussion the inclusion of advance payments in rate base. See, *e.g., Natural Gas Pipeline Company of America,* Order Approving Settlement Agreement with a Condition, Docket No. RP72-132 (July 18, 1973); *Southern Natural Gas Company,* Order Approving Rate Settlement with Condition, Docket Nos.

proved front-end advances made by Transco without question, and accepted the conclusion of the Administrative Law Judge that the existence of the advance payment program was an operative fact of life and hence (47 FPC at 301-2),

> whether or not without the Commission's general sanctioning of advance payments, such payments by Transco would have been necessary in order for that pipeline to secure additional supplies of gas, it is abundantly clear that at this point of time they are Transco's only effective means of competing with other pipelines for such additional supplies. [footnote omitted] For Transco, then, as put by Mr. Stanwood at Tr. 56, 'the name of the game today is advance payments.'

Since, as indicated above, there was no prohibition against front-end advances, Tennessee agreed to make front-end advances on competitive terms in order to obtain needed commitments for gas supply. Under such agreements, Tennessee obtained commitments from producers which were estimated to provide 2.8 trillion cubic feet of gas reserves, equal to almost three years sales (JA 84). Absent these front end-advance payment agreements, these estimated gas reserves would not have been committed (JA 199). Additionally, Tennessee was able to realize substantial cost benefits by agreeing to front-end advances, as against advances made at the time of each producer expenditure. Under Tennessee's agreements, the producers agreed to front-end advances which in the aggregate were $110,000,000 below their estimated producer ex-

RP72-91, *et al.* (July 23, 1973); ***Michigan Wisconsin Pipe Line Company,*** Order Approving Rate Settlement, Docket Nos. RP72-118, *et al.* (July 24, 1973).

penditures with the result that amounts which would otherwise have been recoverable by Tennessee from its customers were substantially reduced (JA 84, 200, 210).

B. The Proceedings Below

In his Initial Decision, the Presiding Administrative Law Judge recommended that the Commission reject the Commission Staff's proposal that an advance-expenditure temporal relationship be imputed in administering Order No. 465. In rejecting the Staff's position, the Judge held (JA 311):

> In light of the careful review by the Commission [in Order No. 465] of the arguments in favor and in opposition to the principle of including advance payments in natural gas company rate bases, and the detailed consideration given by the Commission to the various proposals of interested parties concerning this matter, *it is apparent that if it were the intention of the Commission to restrict the interval between the time that a payment is made, and the time that the funds are expended, the Commission would have so specified by explicit language.*[11]

However, in its Opinion Nos. 769 and 769-A (App. B and C), the Commission (none of whose members were on the Commission when Order No. 465 was issued) overruled the Presiding Judge's Initial Decision, adopted the Staff's position and excluded from Tennessee's rate base more than $100,000,000 of advances made by Tennessee to producers. While the Commission acknowledge that "there is no specific prohibition against [front-end] advances," it held that "such a prohibition is implicit in the 'reasonable

[11] Emphasis is supplied unless otherwise indicated.

and appropriate' standard of these orders" (App. B, p. 104a). Recognizing that its decision was in conflict with an earlier Commission decision in *Columbia Gas Transmission Company, supra,* where the Commission (consisting of members who had considered and adopted the advance payment orders) had rejected a similar Staff position, the Commission held that it was overruling the earlier opinion to the extent in conflict with this opinion (App. C, p. 168a).

In his dissent Commissioner Holloman agreed with Tennessee as to the absence of any advance-expenditure timing requirement and Tennessee's good faith reliance thereon in making its advances, observing, *inter alia,* that (App. C, dissenting op., pp. 197a-198a)

> [advance payments] arrangements [such as Tennessee's] were entered into by the pipelines at the express invitation of the Commission. For the plain fact is this program was thrust upon the pipeline companies, leaving them little choice but to negotiate for these arrangements or abandon the field to competing pipelines. Obviously, considered in the context of growing curtailments and deteriorating gas supply, the latter course would have evidenced a willful disregard of Tennessee's responsibilities to its customers bordering on negligence. *When viewed in the context of the times the Commission's often stated intent that the advance payment program was a novel and experimental one designed to give the participants a free reign and the widest latitude in fashioning workable arrangements; the actual and constructive notice to the Commission of the massive and ongoing nature of these front-end contracts; the common knowledge within the industry that these unlimited front-end advances were 'the name of the game;' and in light of the record evidence in this case, these advance payments are clearly within the 'reasonable and appropriate' standard of Order No. 465 and should be included in rate base. Clearly, this Commission cannot give retroactive application to its current notions as to what a past Commission should have said or done.*

In its decision below, the court expressly recognized that the "advance payments order did not specify the permissible interval between the advance and its appropriate expenditure" (App. A, p 17a) and that Order No. 465 was devoid of any "explicit reference to the timing issue" (*Id.* at 54a-55a). Nevertheless it held that an advance-expenditure timing requirement was implicit in the "reasonable and appropriate" standard of Order No. 465 on the basis of the so-called "used and useful" principle, but that the Commission's 30-day rule was unsupported. Although the court acknowledged that the advance payment program was itself admittedly a departure from the "used and useful" principle, it concluded that there had not been a sufficient affirmative authorization of front-end advances to justify a departure from that principle (App. A, pp. 29a-31a). Further, holding that such rationale "allowed [it] to bypass" the claims of good faith reliance by Tennessee (*Id.* at 32a), the court held that imposition of a reasonable time requirement did not constitute retroactive rulemaking within the exception set out in *N.L.R.B.* v. *Bell Aerospace Co.,* 416 U.S. 267 (1974) (*Id.* at 44a).[12]

[12] The court also affirmed the Commission's treatment of advances to Canadian producers for gas supply and remanded the Commission's decision on rate of return (App. A, pp. 56a-60a). If the Court grants this petition, Tennessee reserves the right to shows that the court below also erred on these matters.

While Judge Wilkey concurred in the court's decision, he observed, *inter alia,* not only that Order No. 465 was "ambiguous," "cryptic," and suffered from "a lack of clear regulatory guidance" (App. A, concurring op., p. 67a) but that (*Id.* at 66a):

> The Commission bears much responsibility for this situation for the opacity of the Commission's orders on the issue of permissible timing could only have contributed to the disruptive effect of advance payment bargaining on the otherwise tightly metered minuet of producers, pipelines, consumers, and regulators. (footnote omitted)

REASONS FOR GRANTING THE WRIT

As matters now stand, the holding of the court below as to Tennessee's Order No. 465 advance payment agreements is directly and clearly in conflict with the subsequent decision of the Fifth Circuit in *United Gas Pipeline Company* v. *F.E.R.C., supra,* also dealing with, *inter alia.* Order No. 465 advance payments.[13] Further, the rationale for the court's holding that imposition of an implicit timing requirement is not impermissible retroactive rulemaking also conflicts with the Seventh Circuit's earlier decision in *Natural Gas Pipeline Company of America* v. *F.E.R.C.,* 590 F.2d 664(1979), albeit the Seventh Circuit decision dealt only with Order No. 499 advance payment agreements.

Proper resolution of this conflict is of critical importance to the natural gas industry as well as to Tennessee as it involves the ultimate disposition of sub-

[13] By Order of October 29, 1979, in Case No. A-362, the Solicitor General, on behalf of the Commission, was granted an extension of time in the *United* case in which to file a petition for a writ of certiorari to and including January 5, 1980.

stantial Order No. 465 advance payments made by interstate pipelines generally. As stated earlier, almost 99 percent of the total of $5.5 billion committed by interstate pipelines under the advance payments program was of the front-end type involved in this case (App. A, p. 21a). Moreover, the problem is of continuing importance. As recognized by the court below, although the program has now been terminated prospectively as to new agreements, "the advance payment contracts retain their vitality, and continued administration is required as pipelines file with FERC for jurisdictional rate increases" (App. A, p. 12a) (footnote omitted)."[14]

1. The Fifth Circuit's decision in *United,* as in the instant case, involved advance payments made under Order No. 465 as well as advances made under Order No. 499. Citing and quoting from Opinion Nos. 769 and 769-A here involved, the Commission in the United rate case, as here, excluded from United's rate base those advance payments remaining unexpended more than 30 days after the close of the test period even though at the same time it acknowledged that the advances had been prudently made and were not unwise from a business standpoint.[15] On review the Fifth Circuit specifically reversed the Commission's order as

[14] In this regard, the Solicitor General in his Application for an Extension of Time in *United* (*supra,* n. 13) recognized the continuing importance of the question (Application, pp. 2-3): "Although the advance payments program was terminated in 1975, the extent to which various payments previously made should be included in pipeline rate base involves very substantial sums."

[15] *United Gas Pipeline Co.,* Opinion Nos. 815 and 815-A, Docket Nos. RP74-20, *et al.,* issued July 29, 1977 and November 15, 1977, respectively.

to Order No. 465 advance payments, stating (597 F.2d at 585-86):

> Creating the impression that it was regulating the particulars of the program, the Commission modified and clarified its initial advance payment order several times between 1970 and 1973. None of these modifications, however, specified a concrete timing relationship between pipeline's advance and producer's expenditure.
>
> As a result of the Commission's program, advance payments became an accepted practice, indeed an essential tool.
>
> . . . .
>
> The Commission's [Order No.] . . . 465 . . . provided no detail, or even broad explanatory statements, instructing the pipelines regarding a payment-expenditure relationship. The first time they really announced this requirement was in Opinions 769 and 769-A. The law will not tolerate this sort of after-the-fact, in fact retroactive, imposition of standards. (footnotes omitted)

Accordingly, the Fifth Circuit reversed the Commission's holding as to Order No. 465 advances in implementation of the court's conclusion that it would be improper to impose any timing requirement with respect to Order No. 465 advances. At the same time, the court reversed and remanded the Commission's application of the 30-day rule to Order No. 499 advances since, as the Fifth Circuit noted, "that order did impose some timing requirement" (597 F.2d at 587).

2. The decision below also conflicts with the Fifth Circuit's *United* decision as to the standards to be applied in evaluating claims of improper retroactive rulemaking under this Court's decision in ***N.L.R.B.*** **v.** ***Bell***

Aerospace Co., supra. **In** ***Bell Aerospace,*** **this Court indicated that an agency has discretion retroactively to apply a new interpretation of an existing rule only when "the possible reliance of industry on the Board's past decision . . . does not require a different result" (416 U.S. at 295). Thus, the Court noted that an agency cannot retroactively impose a new rule when (*Id.*)**

> the adverse consequences ensuing from . . . reliance [on the Board's past decisions] are so substantial that the Board should be precluded from considering the issue in an adjudicative proceeding . . . [and when] some new liability is sought to be imposed on individuals for past actions which were taken in good-faith reliance on Board pronouncements.

The Fifth Circuit in *United* applied this limitation on the Commission's discretion to the imposition of a timing requirement in the advance payments program and explicitly held that "the Commission's action . . . falls within the exception contemplated in *Bell Aerospace*" (597 F.2d at 588). The Fifth Circuit thereby found that the Commission's announcement of a timing requirement for Order No. 465 advances in an adjudicative proceeding was a "retroactive imposition of standards" which, because of the good-faith and reasonable reliance by the pipelines on previous Commission actions, resulted in adverse consequences so severe as to warrant a reversal of the Commission's attempt to give the timing requirement retroactive effect.

The Seventh Circuit in *Natural, supra,* similarly rejected the Commission's attempt to impose a rigid timing requirement as a prerequisite to including advances made pursuant to Order No. 499 in rate base, holding instead that the various pipelines had made

the tremendous amount of advance payments involved in good-faith and justifiable reliance on Commission actions and decisions and that the retroactive imposition of a rigid timing rule could therefore not be permitted (590 F.2d at 669).[16] Accordingly, as in *United,* the Seventh Circuit in *Natural* concluded that the situations presented "come within the exceptions elucidated by the Court in *Bell Aerospace Co.*" (*Id.*):

> The consequences to the appellant of denying rate base treatment to the advances are very severe. It would mean the imposition of a large liability with regard to the advances in the present case. Furthermore, the appellant's entering into these agreements, under these terms, was in reliance upon the prior orders of the Commission, and the policies reflected in those orders, specifically the policies encouraging the advance payment program, with few restrictions, and the promulgation of a flexible standard with regard to the advance-expenditure time relationship.

The decision below admittedly conflicts with the Seventh Circuit's holding as to the applicability of the *Bell Aerospace* exception (App. A, pp. 44a-45a):

> We differ from the Seventh Circuit in that, in our approach, the Commission's current interpretation of the limited purpose of the advance payment order does not reverse a policy that had been the subject of reasonable reliance.
>
> . . . .
>
> We do not discern the substantial claim of justifiable reliance that is needed to invoke the *Bell Aerospace* exceptions. (footnote omitted)

[16] Order No. 499, as noted *supra,* p. 7, contained for the first time in the advance payments program, an advance-expenditure timing requirement which prescribed that the advance must be expended by the producer within a "reasonable time" (50 FPC at 2115).

3. The court's disagreement with the Fifth and Seventh Circuit decisions as to the applicability of the *Bell Aerospace* exception rests on its view that, even though Order No. 465 did not expressly preclude front-end advances, pipelines should somehow have perceived such a prohibition from the "precept . . . that an item may be included in rate base only when it is 'used and useful' in providing service" (App. A, pp. 29a-30a, 38a). In this connection, the court claims that pipelines relied only on Commission "silence" as the basis for their actions in making front-end advance payment agreements, and that such reliance is not sufficient to require application of the *Bell Aerospace* exception; however, Judge Wilkey notes that (App. A, concurring op. p. 67a n. 14):

> [I]t is only with some difficulty that we conclude that 'agency silence' on the issue of timing of advance payments did not convey a tacit and irreversible assurance that advance payments would be upheld if made in full view of the Commission and in arguable compliance with the Commission's ambiguous regulations.

The fact is, moreover, that it was not just Commission silence on which the pipelines relied in concluding that the Commission did not intend to impose a timing requirement for Order No. 465 advances. In the first place, as mentioned earlier, the comments filed by the Public Service Commission of New York in response to the then-proposed Order No. 465 specifically called the Commission's attention to the magnitude of the advances being made "at once" by the pipelines, and urged the Commission to establish provisions which would tie the advances to be included in the rate base to "specific drilling cost expenditures" (J.A. 262-64,

268). As noted *supra,* p. 7, the Commission not only declined in Order No. 465 to adopt New York's proposal but on rehearing rejected New York's renewal of that proposal.

That rejection is clearly more than just silence, particularly since the data which the pipelines had filed with the Commission along with copies of their advance payment contracts, and which the Commission compiled in an Appendix to Order No. 465, showed that many hundreds of millions of dollars had been advanced by pipelines to producers. The sheer magnitude of the advances plainly demonstrated to those familiar with producer exploration and development activities, such as the Commission and its Staff, that the bulk of the advances were being made on a front-end basis. As noted by Judge Wilkey (App. A, concurring op., p. 65a):

> [A]ll available information suggests that the high degree of administrative, judicial, and public scrutiny afforded the advance payment program made the terms of the vast majority of advance payment contracts well known to outside parties, and *certainly to the responsible regulators.* (See also, Commissioner Holloman's dissenting opinion in Opinion No. 769-A quoted *supra*, p. 10).

Secondly, in *Transcontinental Gas Pipe Line Corporation, supra,* the first litigated case dealing with the advance payments program and involving payments under Order No. 410, the Commission agreed with the Administrative Law Judge in rejecting the *only advance-expenditure limitation* which had been proposed, that of *physical,* and *not temporal* proximity (47 FPC at 295-300). In so doing, the Commission continued its clear recognition of the realities of the advance payments program and of the pipelines' utili-

zation of the program to obtain additional gas supplies which it had earlier articulated as follows:

> Transco is competing for gas supply with other major pipelines such as Southern Natural Gas Company and Natural Gas Pipe Line Company of America, which have been allowed to recoup advance payments through rate base adjustments pursuant to our Order Nos. 410 and 410-A. *North Carolina's argument that Transco's advance payments are not reasonable, necessary or appropriate efforts to obtain gas supply are thus without merit.*[17]

Third, in providing an advance-expenditure timing requirement *for the first time* in Order No. 499, issued after Tennessee's Order No. 465 advance payments here involved, the Commission emphasized that that requirement was new and was to be applied prospectively only (50 FPC at 2115, 2118). The Commission characterized its action as being the *establishment* of a "general policy to deal with this issue" (50 FPC at 2115). Obviously, if the Commission already had such a policy, there would have been no need to establish such a policy in Order No. 499. See also *Public Service Commission for the State of New York* v. *F.P.C.,* 511 F.2d 338, 344, 355 n. 15 (D.C. Cir. 1975).

Finally, in *Columbia Gas Transmission Company,* Opinion No. 722, *supra,* issued after Order No. 499, the Commission rejected a proposal to exclude from rate base front-end advances made by Columbia under Order No. 441. While the Commission noted that a timing requirement had subsequently been imposed by Order

[17] *Transcontinental Gas Pipe Line Corp.,* Order Approving Amendment to Agreement as to Rates, Docket No. RP71-31, pp. 2-3 (July 30, 1971).

No. 499, the Commission expressly recognized that there was no basis for invoking such a requirement retroactively for advance payments under Order No. 441 (53 FPC at 712). Significantly, Opinion No. 722 was written by then Chairman Nassikas, who was on the Commission when the advance payment orders were adopted.

In sum, the view of the court below that the pipelines have relied on Commission silence and that there was an implicit timing requirement in the Order No. 465 is not only contrary to all the foregoing, but is contrary to the reading of that order by virtually the entire pipeline industry, by numerous Administrative Law Judges who heard these cases,[18] by the Public Service Commission of New York which actively participated in the advance payment rulemakings from their inception, by the Commission members who were on the Commission when the advance payment orders were adopted, and now by the Court of Appeals for the Fifth Circuit.

4. The court below also erred in invoking the "used and useful" principle, thereby bypassing Tennessee's

[18] See, *e.g.*, *Michigan Wisconsin Pipe Line Co.*, Initial Decision, Docket Nos. CP70-22, *et al.* (February 27, 1976), reversed by the Commission by order issued June 3, 1977, review in D.C. Circuit (No. 77-1719) consolidated with the instant case; *Transcontinental Gas Pipe Line Corp.*, Initial Decision, Docket Nos. RP74-48, *et al.* (December 22, 1975), reversed by the Commission by Opinion No. 801 issued May 31, 1977, review in D.C. Circuit (No. 77-1712) consolidated with the instant case; *Natural Gas Pipeline Company of America*, Initial Decision, Docket No. RP73-110, reversed by the Commission by order issued June 3, 1977, review in Seventh Circuit in *Natural, supra; Trunkline Gas Co.*, Initial Decision, Docket Nos. RP72-23, *et al.* (November 13, 1974), reversed by the Commission by order issued June 3, 1977, review pending in Fifth Circuit in No. 79-1331.

extensive demonstration of good faith reliance. In addition to the fact that the "used and useful" principle is not relied on in any way in any of the Commission opinions here involved and hence, under well-established principles, may not be invoked by the courts to support the Commission's actions here (see, *e.g.*, *F.P.C.* v. *Colorado Interstate Gas Co.*, 348 U.S. 492, 500-01 (1955), and cases there cited), the court's present reliance on the "used and useful" principle does not in fact support its result.

The fact of the matter is that the timing requirement implied by the court below relates to the timing of the expenditures of the advances by the producer-recipient *vis a vis* the advance itself. It has no relationship, however, to the time, if any, such gas is discovered or, *a fortiori,* to the time that such gas, if any is discovered, is in fact attached to the pipeline's system. Only at that time do actual benefits accrue to the pipeline's customers.

Moreover, since, as the court below repeatedly recognized, the advance payment orders themselves constituted a departure from the used and useful principle (see, *e.g.*, App. A, pp. 31a, 43a), even if it is otherwise applicable it follows that the extent of the departure is to be determined from the advance payment orders independently of—and not in reliance on—the "used and useful" principle (App. A, pp. 9a, 31a, 43a; concurring op., p. 63a n.2). This is particularly so since, as Judge Wilkey points out in his concurring opinion (App. A, concurring op., p. 67a), it would be incongruous to hold the pipelines bound by principles from which the Commission itself has departed. In other words, contrary to the holding of the court below that the terms of the departure from the used and useful principle were very

strictly defined, the only provision of Order No. 465 which might be regarded as defining such terms was the "reasonable and appropriate" provision of the order and it is precisely that provision, and its vagueness, coupled with the Commission's own actions, which, as shown earlier (*supra,* pp. 12, 14) formed the basis for the pipelines' good faith reliance on front-end advances being within the intent and coverage of the advance payments program.

In any case, Tennessee's advance payment agreements in fact fully satisfy the used and useful principle. Tennessee's advance payments under Order No. 465 enabled it to add some 2.8 trillion cubic feet of estimated gas reserves that would not otherwise have been available to the system absent such advances (JA 84, 199). Absent such supply, Tennessee's system would not only have experienced even greater curtailments of service to consumers, but increased unit fixed costs due to lower throughput (JA 200). In addition, by agreeing to front-end advances, Tennessee was able to negotiate agreements calling for advance payments which were some $110,000,000 *less* than the estimated aggregate producer expenditures, thereby producing a significant economic benefit for Tennessee's customers (JA 84, 200, 210). Finally, Tennessee's agreements encouraged producers to commit larger tracts, permitted faster development because of the greater amount of capital readily available to the producer, and enabled Tennessee to gain commitments of onshore intrastate reserves during a period when the bifurcated regulatory structure was effectively excluding interstate purchases from the intrastate market (JA 210). Plainly, in any

meaningful sense, the advances here in question were used and useful.[19]

5. The Fifth Circuit in *United* is not only correct in holding that the Commission's imposition of a timing requirement as to Order No. 465 advances is an impermissable "after-the-fact, in fact retroactive, imposition of standards" (597 F.2d at 586), but it is also correct in emphasizing the Commission's responsibility to set forth clear guidelines, particularly in a program such as this where pipelines were urged to make literally billions of dollars of advance payments to producers to encourage the development of gas supplies. The Commission's responsibility to set forth clear guidelines was emphasized in *F.P.C.* v. *Texaco, Inc.,* 417 U.S. 380, 393, 395-396 (1974), where this Court rejected the Commission's attempt to regulate small producer rates indirectly through scrutiny of those costs in pipeline rate proceedings, and was criticized for its failure to state the standards necessary to judge pipeline expenditures with sufficient clarity. As stated by the Fifth

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[19] The court below also intimated that, since capital formation was the central purpose of the advance payments program, the pipelines must have misunderstood this purpose in making front-end advances. This conclusion, however, can only be supported by an assumption that front-end advances are *per se* in conflict with the capital formation purpose of the advance payments program. However, as pointed out in the concurring opinion, the front-end nature of the advances has little direct bearing on the question of whether the advances are consistent with the purpose of capital formation (App. A, concurring op., p. 69a). Thus, the Court's assumption cannot be supported and its conclusion must be rejected.

Circuit in *Highland Resources, Inc.* v. *F.P.C.*, 537 F.2d 1336, 1339 (1976),

> [p]arties should not be put to the task of ascertaining to their peril what the Commission regards as prudent action. They are entitled to rely on published pronouncements of the Commission as to what action they need or need not take.

Clearly, if the Commission had intended to impose a timing requirement in Order No. 465, it had ample opportunity to do so and in fact was urged to do so, but deliberately chose not to. It should not now be permitted after the fact to impose such a standard to deny pipelines recovery of their costs in making these advances.

CONCLUSION

For the foregoing reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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December 19, 1979